



The Impact of SMEs on Economic Development of Bangladesh

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ABSTRACT

The growth of the economy can be attributed to the positive shifts - from agricultural-based to industrial-based, from input-driven to productivity-driven, and from traditional to knowledge-based-technology-orientated economy. Small and medium enterprises (SMEs) have been playing an essential role in the development of the economy of Bangladesh, and it can be claimed that it is the backbone of industrial development in the country. This paper attempts to discuss the extent to which the economy has benefited from the expansion of the SME sector and identifies the contribution of the SME Foundation in the process of uplifting and flourishing SMEs. The SME Foundation has been doing a remarkable job in this regard with continuous endeavors to facilitate innovation of new products, the introduction of new production technologies, marketing of goods and services, skills development training, advocacy, policy formulation, and linkage with national and international organizations. The study reveals that the development of the SME sector played a major role in contributing to the economic growth through providing support to the existing SMEs, creating non-traditional opportunities, generating employment, making the labor force more skilled and effective through training, enhancing labor productivity, and improving product and services quality. SMEs are accounting for 25% of the GDP of Bangladesh and 80% of total industrial jobs; and therefore, significantly has been contributing to 6% to 8% of the economic growth rate in the last decade.

Keywords: *Bangladesh, Economic Growth, Small and Medium Enterprises (SME), SME development*

INTRODUCTION

Bangladesh is faced with a long list of complicated Econ-political problems inherited from the past and very few effective measures have been undertaken by the concerned organizations to remedy these problems, to create a favorable climate for industrialization. These, in turn, have led to poor economic growth, low ca pita income and sub-human living conditions. Though the agriculture in Bangladesh faces several adverse conditions for development, it is still the pivotal sector, around which rests the national economic development. To stimulate any development in agriculture, industrial development, particularly large scale industries are essential and this would also help the development of a sound industrial base. At the same time, contribution from the small and medium industries to the economy of Bangladesh is significant even at present and the future potential too, is great. Unfortunately, this sector of industries faces numerous bottlenecks like inadequate and inefficient infrastructure, inappropriate policies and actions of government, lack of effective implementation of policies, inefficient development institutions, inadequate financial assistance, absence of special financial institutions, and problem concerning labor, entrepreneur, technology, and market. Though such problems are common both for small and medium industries and the large industries, due to lack of power and resources, the former is affected more than the later.

Two among the innumerable problems particularly stand out, being primary elements of development. These are literacy and lack of adequate and efficient infrastructure. Government has to direct all its efforts in tackling these two basic issues as early as possible; as such efforts will pave the way for easier handling of the issues.

The BSCIC should be allowed to operate as a real autonomous body with ample resources and appropriate manpower. In spite of the several criticisms lodged against the BSCIC, it is not completely failed in discharging its responsibilities. It has all the potentials to act as a prime institution for the promotion and development of small and medium industries. Institutions for the train of workers and entrepreneurs should be encouraged to utilize existing resources to their optimal capacity and efficiency. A special financial institution for the small and medium industries should be created as soon as possible and during the transition period, the existing facilities of BSCIC and nationalized commercial banks need to be encouraged to create special units in their organizations to attend to the special needs of these industries. Consultancy and advisory services by capable people have to be created and delivery of services should be a full package of assistance covering technology, finance and marketing.

The macro economic reforms and management in key economic sectors have significantly influenced the growth in different economic sectors of the national economy. Bangladesh, mainly backed by the growth of industry and service sector has achieved a GDP growth of 5.38 percent in the year 2004-05. Per capita GDP and GNI stood at US \$445 and US \$470 respectively. The rate of national investment rose to 24.43 percent, which is the ever highest. The contribution of private sector to this investment is 18.53 percent. The contribution of the private sector to the economy is increasingly becoming prominent. In the year 2004-05, the growth of credit to the private sector stood at 17.20 percent. The average inflation stood at 6.49% in the year 2004-05. The population growth rate (as percentage) for the year 2004 stand for 1.5 and the literacy rate for this year 2004-2005 stand for 62.66 percent.

SMES in Bangladesh

In a note about issues of SMEs' access to finance, to nothing about the SMEs in Bangladesh may appear to some evocative of "having Hamlet without Caeser". It is to address that essential balance, this appendix distils some evidence recently analyzed by the SME Cell. Much of the information is based on the data generated by the 2001/2003 Census of enterprises carried out by Bangladesh Bureau of Statistics (BBS).

Current Status of the SMES in Bangladesh

(a) In 2001/2003, there were about 78,400 small and medium enterprises (SMEs) in Bangladesh not counting those in public administration and defense. Small and medium scale of establishments account for some 93% of all establishments with in excess of a head-count of at least 10: they account for some 44% of the corresponding employment. The SMEs clearly represent one capstone of the industrial landscape of Bangladesh, some 3.5 million workers employed in the sector.

(b) Urban Bangladesh accounts for some 60% of units and 76% of employment overall in the SME enterprise sector, with rural Bangladesh accounting for the rest. Ninety-three point three (93.6%) of all units in Bangladesh belong in the SME category, i.e. have between 10 and 99 employees. However, SMEs account for only 44% of the total employment of the enterprise sector.

Employment per establishment within each of "small", "medium" classes in 2001/2003 suggests very considerable heterogeneity in the scale of productive capacity as between "small" and "medium". What is the point of bringing this recognition at this stage? The average employment per establishment is 18 workers or so. The corresponding average employment for medium enterprises falls in a narrow range of between 65–69 employees. The average medium establishment in Bangladesh's SME sector is more than 3.5 times the size of the corresponding small establishment. Policy-making within the framework of PRSP must note this schism.

Evidence from the BBS concerning the number of SMEs (on the BBS definition) underlying BBS' Census of Manufacturing Industries (CMI) shows that small establishments (those with head-counts of between 10 and 49 workers) face substantively different "dynamics of growth" compared with medium establishments. The number of establishments in each of the two smallest, the most populous size-classes, has substantially shrunk between 1991/92 and the year 2000. The number of medium establishments has nearly trebled in the mean time: the increase is on the order of 191%. For comparison, the number of large enterprises overall grew by 111% during this period.

While it is quite admissible to use "SMEs" as "policy refrain" to legitimize a purposeful separation between the problems of SMEs compared with large enterprises, it is imperative to remember that "small" and

“medium” are two very different “target groups”. At this juncture, we can do little better than to paraphrase from a classic, from the World Bank. To quote: “A group of people who are not only all vulnerable but also relatively homogeneous with respect to the effect that a given set of policy instruments might have upon them may be defined as a *target group*. This approach requires that the definitions of target groups should, as far as possible, reflect causes rather than symptoms of poverty. With this concept it is possible to take account of the complementarity among policy instruments and hence the need for policy packages. The concept facilitates the identification of specific forms of assets which can improve the conditions of different groups of the vulnerable. The approach also eases the task of assessing the extent to which the benefits of policies will actually reach the target groups” (Hollis Chenery et al, 1973,). With the concern of the PRSP in view, we would like to flag one question for this workshop: “Is it admissible to introduce “small enterprises” (SE) as a valid programmatic category for legitimate intervention purposes, within the corpus of SME policy strategies?”

Table 1.1: Changes in the Structure of Industries between 1992 and 2000 (Based on number of establishments reporting to BBS for CMI)

Employment size classes	1991/92 No. of units	1999/2000 No. of units	Percentage Change
10-19	12644	10480	-17.0
20-49	5546	5470	-1.4
50-99	1326	3839	+190.0
SMEs	19514	19789	+1.0
100-199	593	1828	208.2
200-499	643	2269	253.0
500-999	184	624	239.0
1000+	174	243	39.0
Large	1594	4964	+211.41

Source: SME Cell, 2005, using data from two BBS CMI reports.

Place of SMEs in the National Economy of Bangladesh

Any precise quantitative estimate of the importance of SMEs in Bangladesh economy is precluded by non-availability of comprehensive statistical information about these industries at the national level.

The latest BSCIC estimates suggest that there are currently 55,916 small industries and 511,612 cottage industries excluding handlooms. Including handlooms, the number of cottage units shoots upto 600,000 units indicating numerical superabundance of the SCIs in Bangladesh. Quoting informal Planning Commission estimates, the SMDF puts the number of medium enterprises (undefined) to be around 20,000 and that of SCIs to be between 100,000 to 150,000. This wide variation in the BSCIC and Planning Commission estimates of the numerical, size of the SMEs might be due to at least two reasons: (a) different set of definitions of the SMEs and (b) different coverage of SME families. This strongly suggests the need for adopting and using an uniform set of definitions for SMEs by all Government agencies to help formulation of pro-active SME promotion policies.

Whatever the correct magnitude, the SMEs are undoubtedly quite predominant in the industrial structure of Bangladesh comprising over 90% of all industrial units. This numerical predominance of the SMEs in Bangladesh's industrial sector becomes visible in all available sources of statistics on them (Ahmed, M.U 2001). Together, the various categories of SMEs are reported to contribute between 80 to 85 per cent of industrial employment and 23 per cent of total civilian employment (SEDF, 2003)². However, serious controversies surround their relative contribution to Bangladesh's industrial output due to paucity of reliable information and different methods used to estimate the magnitude. The most commonly quoted figure by different sources (ADB, World Bank, Planning Commission and BIDS) relating to value added contributions of the SMEs is seen to vary between 45 to 50 per cent of the total manufacturing value added.

While the SMEs are characteristically highly diverse and heterogeneous, their traditional dominance is in a few industrial sub-sectors such as food, textiles and light engineering and wood, care and bamboo products. According to SEDF sources quoted from ADB (2003), food and textile units including garments account for over 60% of the registered SMEs. However, as identified by various recent studies, (Ahme, M.U. 2001,

ADB 2001, US-AID 2001) the SMEs have undergone significant structural changes in terms of product composition, degree of 2 The robustness of SME contributions to employment generation is a common phenomenon in most developing countries in that the magnitude varies between 70 to 95 per cent in Africa and 40 to 70 percent in the countries of the Asia-Pacific region (Ahmed, M.U. 1999) capitalization and market perpetration in order to adjust to changes in technology, market demand and market access brought by globalization and market liberalization.

OBJECTIVES OF SME

1. Implementing SME Policy Strategy adopted by the Government of Bangladesh.
2. Recommending SME friendly policies to different government ministries and agencies.
3. Providing business support services to the SME entrepreneurs.
4. Providing information and proper guidance for establishing new SMEs.
5. Conducting sectoral study to ensure availability of latest information, identify challenges and recommend preventing measures.
6. Operating credit wholesaling programs for the SMEs through different banking and non-banking financial institutions.
7. Conducting training programs to create skilled labor for different SME sub-sector based on their demands.
8. Technology development, adopting new technology, conducting reverse engineering and supporting SMEs to get quality certifications.
9. Supporting SMEs in marketing their products and promotion of services.
10. Bringing women entrepreneurs into the mainstream of development and helping them to achieve economic self dependency.
11. Assisting SMEs in creating institutional bondage with foreign companies for capacity building, technology transfer and improving productivity.
12. Training up and motivating SMEs in using ICT tools for more productivity and improving quality.

Activities

Implementation of SME Policy Strategies adopted by the Government of Bangladesh Implementation of the SME Policy Strategies adopted by the Government of Bangladesh is one of the main responsibilities of SME Foundation. SME Foundation continuously assist the government in core issues mentioned in the policy strategy like: recommend rational budget structure for SMEs, advice on fiscal and financial issues, assist to ensure quality of SME products, assist in capacity development, techno-entrepreneurship development, information support through web portal, establishment of virtual SME front office, assist in technology transfer activities at international level etc.

Though the dependence of the economy of Bangladesh on agriculture has been reduced to a considerable extent from 65.2 per cent in 1949-50 to 54.16 percent in 1981-82, still the lion's share of GDP comes from this sector. Around 90 per cent of the population lives in the rural areas and they are directly or indirectly dependent on agriculture for their living. Agriculture is carried on in a most backward and primitive method and production per acre is one of the lowest in the world. In 1969-70, only 4 per cent of cultivable lands were under irrigation in Bangladesh. Hence, agriculture needs to be modernized and its development will continue to dominate the planning process of the country this will call for provision of service facilities to the farmers for their agricultural tools and implements. Locally designed machines and implements will be essential for increased output without causing much damaged to employment. For irrigation purposes there are already more than 44000 low lift pumps in operation. Many of these pumps are locally manufactured and service facility for their maintenance. These will a large number of repair shop and manufacturer for manufacture of spare parts and components throughout the country. Since the capacity of pumps vary and the area of usage dispersed, SME repair shops and spare parts manufacturing factories have come up in large numbers in the various parts of the country. This development is the natural outcome of the requirement of the market. Large scale industries can not profitably operate in such cases and deliver goods within a short time. Recognizing the importance of SME in the process of modernization of the agricultural sector, the government has decided to encourage the development of such industries.

If the surplus agricultural workers, landless rural workers, and unemployed millions in the villagers in Bangladesh are to be engaged in some productive occupation, the employment creation must be through the

promotion of SME in rural areas of Bangladesh. Promotion of large industries in urban areas and creating employment will intensify the common urban problems already existing there. It is important that in a predominantly agricultural country like Bangladesh, the pattern of industrial development should be in close support of the agricultural development and vice versa. Due to an inadequate and inefficient transport network in the country and the small size of the country, this objective can best be served by the SME and especially for agro-implements and spare parts. The seasonal character of the agriculture of Bangladesh leaves the cultivators without works for a considerable period of the year. The SME can provide them job opportunities during the slack periods. Thus considering the nature of the rural Bangladesh, the promotion and development of SME is the only way out for solving the typical rural related problems of Bangladesh. This is also applicable to other countries similar to Bangladesh.

SMEs are recognized as engine of economic growth and employment generation for sustainable industrialization in both developed and developing countries of the world. In context of Bangladesh, there is no alternative of small and medium enterprises for rapid industrialization and national economic growth through lower capital investment and employment generation. The SME Foundation is playing its role in helping the SME entrepreneurs including the women entrepreneurs by conducting various programs with an aim to develop the SMEs of Bangladesh. One of the major aims of SMEF is to bring the grassroots entrepreneurs into the main stream of economic development through employment generation, reduction of social discrimination and poverty alleviation.

Role of SMEs in the National Economy

Bangladesh has liberalized conspicuously throughout the 1990s. As a result of this broad liberalization, the overall orientation of trade policy in Bangladesh has altered considerably, in the process becoming significantly less protective and less biased towards import substitution activities and therefore less discriminatory against domestic exporters (and potential exporters). During the 1990s, the coverage of quantitative restrictions fell from 253 four-digit Harmonised System (HS) codes to 28, while the average tariff actually applied (based on total revenue collections) fell from 62.3 per cent to 23.0 per cent. Maximum customs duty declined from 350 per cent to 25 per cent during this period. In other words, Bangladesh has been a poster child of good, even docile, management of its trade and industrial policies.

Has this great effort yielded commensurate gains in terms of growth rates? The growth rates of the GNP, the manufacturing value added, and trading sectors in the Bangladesh economy for four overlapping quinquennial periods beginning from 1976/77 up to 2003 shows no evidence at all of a significant quickening of the rate of economic growth in any of the three growth indicators. Whereas, the differential between the rates of border taxation between the two period is highly significant. The clear implication is that trade liberalization is a necessary but no means sufficient condition of a significant acceleration of growth rate of any given developing country.

This is not the place for a fully-blown analysis of Bangladesh's trade and industrial policy. What we want however to do at the present time is to emphasize that with the dismantling of the protective tariff structure, Bangladesh has become more outward-looking in how it sources its requirements for various products. An obvious by-product of that trend has been that domestic manufacturing for domestic absorption in which especially small and medium firms have a natural interest may well have declined. Business interest in making a quick profit from indenting and trading has been piqued, while successful domestic manufacturing has become very challenging indeed.

It is in this context that the recent policy interest in the SMEs has to be seen. In country after country, leaders have come to the conclusion that while accelerated trade liberalization is a necessary condition for creating an enabling environment for the broad-based growth of the manufacturing industries, the small and medium enterprises will require well-targeted assistance package, especially in terms of credit availability, skilling-up and mentoring on how to make most of the opportunities that an outward-looking regime of trade and industrial policies can unleash. This recognition has been instrumental in spawning in the recent times an urgent and sustained interest in the SMEs as building blocks of adjusting to the radically different market and policy scenarios in the post-liberalization era in Bangladesh.

It cannot, of course, be gainsaid that rapid trade liberalization has a knack for providing globally companies or globally-branded countries (such as China and India) a breakthrough for well-orchestrated penetration by their own products into debt-dependent countries in which SMEs are still in their infancy. Their capitulation is quick before the avalanche of imports of products from globally-branded competitors, at times from prices that suspiciously look like dumping, from countries that typically are capital-surplus. (A lot of the penetration by imports into Bangladesh by China and India in several lines of products is due to the formidable marketing clout of firms in the latter, not necessarily because the product was always of superior quality or most cost-effective.) Consequently, imports of the liberalizing countries can grow much faster than their exports ever can, given the non-price market barriers in the developed countries. In Bangladesh, imports payments have grown at a rate of 24% between 1988/89 and 2002/3, while exports have only grown at a rate of some 17% annually. The differences between those two growth rates are statistically highly significant.

While liberalization may well have created opportunities for gainful growth through trade on the demand side, such gains, going forward, must be seen as counterbalanced by formidable challenges on the supply side. First, competition has become increasingly fierce among the global and regional economies and enterprises, SMEs included. There are also many more producers competing for both existing and new markets and market segments for goods, services, finance and other wealth-creating technologies and knowledge. The competitive strength of China was notable in the above regard, even before the country became a member of World Trade Organization in December 2001. Indeed, market penetration and displacing pressures from China have been keenly felt by producers across Asia, particularly those suppliers (including SMEs) at lower stages of technology sophistication and relying on high import content. At the same time, the fairly meteoric ascendancy of India since the turn of the century as a magnet for direct foreign investment (DFI), and the outsourcing of much design and development work from the OECD countries in industries as diverse from movie-editing to chip-design, is a sign, increasingly ominous for competitiveness, of the present times.

Second, consumer preferences and market standards have become more sophisticated and exacting. Competitive advantage is now determined by several non-price parameters such as quality, health and safety, social equity in employment and production, and ecological compatibility of products and processes. Furthermore, market demand is constantly changing, a trend facilitated not least by the rapid advances in ICT, bio-engineering and new materials. In consequence, there are more frequent introductions of new products and processes, faster and more innovative design changes, shorter product cycles and smaller output batches, higher quality and greater mass customization, more just-in-time sourcing and greater punctuality in delivery. This is the context in which we have to draw up a strategy for reviving the flagging SME sector in Bangladesh.

Role of SMEs in the National Economy of Bangladesh

According to UNESCAP, SMEs account for upwards of 90% of all firms in East and South-East Asia, as well as in Japan (Wattanapruttipaisha, 1999). It is also the biggest source of the region's employment, including three-quarters of the region's employment, in particular its women and young workers. The relative share of SMEs in total output and exports is typically much smaller, close to a third, or so. In Bangladesh, large enterprises account only for a small percentage of all business enterprises. The percentage is much smaller in other than manufacturing than in manufacturing per se.

The manufacturing industry essentially comprises small and medium scale enterprises: by some accounts, 60% and 25%, respectively, of the workforce in manufacturing happen to be hired by small and medium enterprises. It is hardly an overstatement to say that small and medium enterprises are pretty much synonymous with manufacturing industry.

CONCLUSION

SME has been seen as the pivotal forces behind the rapid employment and income generation, increase in the per capita income and brings economic emancipation of the backward and downtrodden section of the society. As such, the contribution of the SME sectors is worldwide acclaimed. In our country the role needs to be played by the sectors are of great significance.

At present SME comprises of 80% of industrial units and 80% of private initiatives and 50% contribution to GDP. Thus, the economic impact of SME cannot be ruled out rather the interactive contribution of SME should be suitably utilized for employment and income generation, growth in the GDP, increase in the economic indicators, increase in the export and alleviation of poverty of the employees and the employers. The benefits of the SME can best be harvested in the following manners;

RECOMMENDATIONS

1. SME is in the initial stage of the form as industries. Strong financial supports from the government as well as the private sectors and international donor agencies must be ensured as a free flow without any constraint.
2. Training for imparting skills on technical aspects, knowhow and technology transfer through a permanent setup. Exclusive training to given on marketing methods and marketing strategy along with the demonstrated target markets. The refinance facility from the Bangladesh Bank must be increased from 2% to 50% with immediate effect and claim of refinance from the disbursing authorities must be settled without any loss of time.
3. Setup Villages for small and medium enterprises in every district near the small and medium enterprises cluster with specific booster enterprises. Government should enact Small and medium enterprises Act to recognize the contribution of small and medium enterprises in the national economy.

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